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April 10, 2002

BY HAND
Mr. William F. Caton
Acting Secretary
Federal Communications Commission
445 12th Street, SW
Washington, D.C. 20554

Re: CC Docket 80-286
Reply of Roseville Telephone Company to Comments of Verizon on Roseville's Petition for Reconsideration

Dear Mr. Caton:

On behalf of Roseville Telephone Company I am enclosing an original and four copies of a Reply of Roseville Telephone Company to Comments of Verizon on Roseville's Petition for Reconsideration.

Should any questions arise concerning this matter, please contact me.

Very truly yours,

Paul Feldman

Paul J. Feldman
Counsel for Roseville Telephone Company

PJF:jpg

Enclosure

cc: Mr. Jack Day
Mr. Greg Gierczak
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of	)	
	)	
Jurisdictional Separations and Referral to	)	
the Federal-State Joint Board	)	CC Docket No. 80-286
	)	

REPLY OF ROSEVILLE TELEPHONE COMPANY TO COMMENTS OF VERIZON ON ROSEVILLE'S PETITION FOR RECONSIDERATION

Roseville Telephone Company ("Roseville"),[1] by its attorneys and pursuant to Section 1.429 of the Commission's rules, hereby replies to the Comments of the Verizon telephone companies, filed on March 26, 2002 in the above-captioned proceeding. Of all of the companies impacted by separations policy, only one opposed Roseville's PFR. Yet, as demonstrated herein, Verizon's argument regarding the availability of reliable data is unpersuasive, its assertion regarding the impact of broadband is speculative and misplaced, and the assertion that the costs of delivering traffic to the Internet are recovered through local rates is just not correct.

I. Introduction

On July 21, 2000, the Federal-State Joint Board issued a *Recommended Decision*[2] recommending that the Commission implement an interim freeze of Part 36 category relationships and jurisdictional allocation factors. The Board properly suggested that such a freeze would provide "much needed simplification and stability to the separations process in a time of rapid market and technology changes." *Recommended Decision* at para. 1. Most

[1] Roseville is a wholly-owned subsidiary of SureWest Communications.

[2] In re Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, FCC 00J-2, released July 21, 2000 ("*Recommended Decision*").

important among the changes in technology that formed the basic rationale for the freeze is the rapid growth in the use of the local network to deliver traffic to the Internet. As the Commission itself noted in para. 39 of the Separations Freeze Report and Order,[3] the "Joint Board's concerns regarding Internet usage stems from the fact that costs for ISP-bound traffic, despite the jurisdictionally interstate nature of this traffic, are booked as intrastate for separations purposes." Accordingly, the Joint Board recommended that if the Commission finds that Internet traffic is jurisdictionally interstate, then the separations freeze should include a freeze of the local DEM factor "at some substantial portion of the current year level ...." *Recommended Decision* at para. 2.[4] While the Joint Board sought comments on what would be the appropriate amount by which the local DEM should be reduced, and recognized that it might be difficult to precisely quantify the proper amount, it did not recommend taking no action if complete precision could not be attained at this moment. Rather, it recommended in that case the use of a default level of 95 percent of the current year level. *Id.* at para. 29.

[3] 16 FCC Rcd 11382 (2001).

[4] The Joint Board recommended that the adjustment of the DEM factors occur at the same time as the freeze. Roseville's PFR sought reconsideration of the Commission's decision not to adjust the DEM factors at the same time that the freeze was instituted. Thus, there is no relevance to Verizon's off-hand comment that "[i]f the Commission were to reallocate separations for every carrier who believed the existing separations balance 'inappropriately shift[s] costs,' separations would never be frozen." Comments at page 2. Roseville is not advocating on-going shifts in the frozen factors, just the one shift recommended by the Joint Board. Accordingly, such action will not "undermine the simplicity and stability offered by the current separations freeze" (as incorrectly asserted by Verizon at page 1), even if the adjustment in the DEM factors occurs in response to the Roseville PFR, rather than when the freeze began.

In response on this issue, the Commission acknowledged that it had recently reaffirmed its finding that Internet traffic is jurisdictionally interstate.[5] It also acknowledged that the record demonstrates "some growth" in local calling patterns, and that it "may be reasonable to assume that some portion of this growth is attributable to increased Internet usage." *Id.* Nevertheless, the Commission chose not to reduce the local DEM factor, because it believed that it lacked "reliable data" upon which to set an amount for reducing the local DEM.

On July 20, 2001, Roseville filed a Petition for Reconsideration ("PFR") of the Commission's decision to decline to reduce the local DEM for the base year of its freeze, and shift that amount to the interstate DEM. In its PFR, Roseville demonstrated that:

1. There is reliable evidence in the record upon which to base a rational reduction in the DEM. Roseville pointed the Commission to the filings made by the National Exchange Carrier Association in this proceeding. NECA's Comments in response to the *Recommended Decision* referenced the extensive documentation made by parties in this proceeding regarding the amount of usage of the local network attributable to the Internet. Those Comments also cited to a 1999 NECA study of 1998 carrier traffic data, revealing Internet usage of approximately 18 percent.[6] The data provided by NECA, alone or in combination with other evidence in the record, provides a reasonable basis for a specific reduction of the local DEM factor.

2. Even if there were an insufficient record to select a factor different than that recommended by the Joint Board, the rational and required approach for the Commission would have been to enact the default figure established in the *Recommended Decision*. The Joint Board's recommended default mechanism did not leave the alternative of no action if the Commission could not obtain absolute precision at this moment. Rather, it recommended in that case at a minimum the use of a default level of 95 percent of the current year level.

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[5] Separations Freeze Report and Order at para.40, citing Intercarrier Compensation for ISP-Bound Traffic, Order on Remand and Report and Order, FCC 01-131 (rel. April 27, 2001) at paras. 52-65.

[6] *See* October 28, 1999 Letter from Gina Harrison, NECA to Dorothy Attwood, in CC Docket 80-286 ("*NECA Letter*").

Verizon was the only party to file Comments in response to the Roseville PFR. As shown below, their Comments provide no basis for denying the PFR.

II. Verizon's Argument That There is No Reliable Basis For Modifying DEM Factors is Unpersuasive.

Verizon asserts that the Commission properly concluded that there is no reliable data upon which to base a revision to the DEM factors. This argument is unpersuasive. First, it states that "the Joint Board has recognized that the portion of local calls that are attributable to Internet traffic is "possibly unidentifiable." Verizon Comments at pages 2-3, citing the Glide Path Paper from the State Members of the Federal-State Joint Board on Separations at page 6, CC docket 80-286 (filed December 19, 2001). Yet, Verizon's quote is taken out of context – surrounding the two words quoted by Verizon is the following:

> It is difficult for carriers to ascertain which local calls are in reality ISP-bound traffic. Thus an unidentified (and possibly unidentifiable) portion of local calling is now jurisdictionally interstate.

When placed in the context of the two surrounding sentences, it becomes clear that the Board primarily believed that it was difficult (rather than "impossible") to ascertain the portion of local calls going to the Internet. And while the Joint Board may have considered such a task to be difficult, that does not mean that it was suggesting that the attempt should not be made. Nor is there any evidence that the two words in a policy white paper were intended by the Board to undercut a core principle of the *Recommended Decision* it enacted the year before.

In following up its out-of-context quote from the *Glide Path Paper*, Verizon goes on to assert that Verizon "like other carriers, does not (and, as a practical matter, cannot) break out the Internet-bound traffic from general minutes." Comments at page 3. Here, Verizon has made much too broad of a generalization. As a price cap carrier, Verizon does not use traffic factors in

developing its interstate access rates, and thus does not have an incentive or need any longer to identify Internet-bound local traffic. However, as a rate-of-return carrier, Roseville has had the incentive and need to identify such traffic in developing rates, and has had experience in doing so.

In identifying Internet-bound traffic, the first step that Roseville took was to survey the local service area to identify the most commonly used ISPs in the LATA. Roseville then researched the web sites of those ISPs to determine the dial-up numbers they use in the local service area. With this information, Roseville performed monthly "point to point" traffic studies using actual recorded call data for every call that originated from a Roseville measured-service customer and terminated to one of the identified ISP dial-up numbers. The evidence from traffic studies on Roseville's network support the conclusion in the *NECA Letter* that 18 percent of traffic on the local loop is carrying date to the Internet. Indeed, Roseville believes that the figure is likely to be greater than that on a national basis.

Ironically, while Verizon claims in this proceeding that carriers cannot as a practical matter break out Internet-bound traffic from other local traffic, Verizon has recently made the opposite argument in a proceeding on reciprocal compensation in front of the California Public Utilities Commission. Therein, Verizon asserted that "it is possible to track ISP-bound traffic with reasonable accuracy" using both statistical approaches and traffic studies.[7] For example, at page 49 the *Verizon Brief* states:

> [a]s Verizon witness Beauvais explains, the average traffic patterns for ISP traffic and local voice traffic are sufficiently distinct to allow a simple algebraic formula to be applied to observed hold-time data to estimate the amount of ISP-bound

[7] *See* September 18, 2000 Opening Brief of Verizon California in CPUC Docket R.00-02-005 (*"Verizon Brief"*). Portions of that *Brief* are attached hereto as Attachment 1.

> traffic travelling (sic) between any two carriers [footnote deleted]. Both the published data and Verizon's own observations demonstrate that the average duration of ISP-bound traffic is much longer than the average duration of typical local voice traffic [footnote deleted] and the standard deviations are such that – even at the 99 percent confidence interval – the confidence intervals do not even come close to overlapping [footnote deleted]. This rather large difference in average duration means that it is possible, as a statistical matter, to distinguish between these two types of traffic with sufficient precision for the Commission's purposes.

Verizon goes on to state at page 51 that:

> [a]ssuming, for argument's sake, that estimates based on conservative hold times alone were deemed to be insufficient for some reason, which they should not be, the parties could still segregate ISP-bound traffic from other forms of traffic by conducting traffic studies that sample traffic flowing between the ILEC and the CLEC. Of course, to conduct such studies, it would be necessary to identify by telephone number the ISPs being served by the parties. Although the CLECs suggest that this would be an impossibility, the record in this proceeding demonstrates otherwise. As a threshold matter, the telephone numbers used by ISPs are widely published [footnote deleted]. Even if they weren't, there is every reason to believe that the parties to this proceeding could readily identify their own ISP customers because carriers need to know whether their customers are ISPs in order to determine how best to serve them.

In sum, whatever the motive that Verizon has in this proceeding for arguing that ISP-bound traffic cannot be identified, it has admirably demonstrated the opposite in a proceeding on reciprocal compensation. In any case, Verizon's argument in this proceeding suffers from another fundamental flaw: even if it were true that there is no reliable way to measure the current percentage of local traffic going to the Internet, the Joint Board did not leave the alternative of no Commission action on the DEM factors. Rather, it recommended that in such a case, the Commission should at a minimum use a default level of 95 percent of the current local factor. Verizon ignores this portion of the *Recommended Decision*, but the Commission cannot do the same.

III. Verizon's Assertion Regarding the Impact of Broadband Traffic is Speculative and Misplaced.

Verizon states that "even if" there were a way to identify the specific portion of local traffic that is attributable to interstate Internet usage in the past, this figure will be irrelevant in the future, because use of the local loop for dial-up calls to ISPs will greatly decline as cable modem and satellite broadband technologies grow in market share. Verizon Comments at page 3. This assertion is speculative and misplaced.

The impact of broadband on growing Internet use is not a zero-sum game: even if there is continued growth in access to the Internet through cable modems and satellite, Roseville has seen an increase of usage of the Internet through the local loop. Rather than broadband leading to less traffic on the local loop, it is just as likely that users that shift from dial-up to other broadband technologies will be replaced with new users of the Internet, who use the less expensive dial-up local loop technology. Thus, Verizon's assertion is misplaced. Furthermore, it is pure speculation to predict the growth and impact of cable modem and satellite broadband technologies. Especially in the case of satellites, history is littered with unfulfilled predictions of tremendous growth.[8] What is certain, however, is that overall Internet use (regardless of access technology) is tremendous and will continue to grow.

In addition, Verizon's broadband argument suffers from the same underlying flaw as its argument that there is no reliable data: even if the Commission believes that the percentage of

[8] For example, the recent bankruptcy filings of satellite providers Iridium and Globalstar should be noted. In addition, EchoStar announced this week that it would no longer act as a wholesaler of the Starband satellite Internet access service. In that announcement, EchoStar noted that the "large number of well-funded companies that have abandoned or suspended their investment in [satellite-based Internet services] highlights the difficulty in establishing [such services]". *See*, "EchoStar Stops Backing Starband After $100 Million Investment", *Communications Daily*, April 8, 2002, at pages 7-8.

traffic on the local loop will decline in the future, the Joint Board did not recommend taking no action on DEM factors in such a case. Rather, it recommended adoption of the default reduction, for the period of the separations freeze.

IV. Assertions That Internet Traffic Costs are Fully Recovered Through Intrastate Charges are Untrue.

Verizon proffers the argument that costs for local traffic delivered to the Internet are properly recovered through business rates tariffed at the state level. Comments at page 4. Yet, as Roseville stated in the PFR, the fact that ISPs are exempted (under FCC policies for enhanced service providers) from paying interstate access charges does not change the interstate nature of the services provided to the ISPs, or the need to recover the cost of those services properly. Verizon responds that use of local business rates does lead to "proper" recovery of these costs, since the costs are matched to revenues collected through intrastate tariffs. *Id.* However, such an argument suffers from two fatal flaws. The first flaw is in the use of a kind of circular logic: the proper jurisdictional allocation of the cost of a service is not determined by the jurisdiction of the tariff used to charge for the service, but rather from the actual jurisdictional nature of the traffic that generates the cost (which in this case is interstate traffic going to the Internet). The fact that ILECs charge for this service using local business rates is not the result of a factual analysis of the traffic, but rather the result of the Commission's "ESP exemption" policy. The existence of that policy does not magically change the true nature of the traffic.

The second flaw in Verizon's argument is that traditional business line rates are not designed to recover the costs associated with delivering data traffic to ISPs and with the length of such calls. Similarly, Internet traffic on residential flat rate lines causes an even greater amount of unrecovered costs. In designing local rates, companies and state commissions take into account

the duration of the average local voice call. For example, on the Roseville network, the duration of the average local call is 6.35 minutes. However, the duration of the average call to an ISP is 25 minutes, a difference of 393 percent.[9]

The increased usage and longer holding times generated by calls to the Internet has resulted in very real costs for Roseville. The company has had to add significant amounts of trunking and switching capacity because as long as a call is connected to the network, the switch is performing functions until the customer disconnects. If Roseville did not add the required capacity to accommodate this increased usage caused by calls to the Internet, eventually there would not be enough trunks and switching capacity to connect calls.

Verizon acknowledges Roseville's point that the intrastate revenues are insufficient to cover the costs, yet asserts that the proposed cure – allocating the costs to the interstate jurisdiction – is worse, since (according to Verizon) there are "no revenues" on the interstate side to cover those costs. Comments at page 4. But Verizon's "no revenues" argument is not only completely unsupported, it is untimely. The issue here is one of revenue requirements. The true costs of delivering traffic to the Internet must be established with the appropriate jurisdiction for cost recovery. When the revenue requirements have been derived, then a determination can be made as to whether additional funding is necessary. If there is a need for additional funding, only

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9 Roseville has reviewed traffic studies of its network performed throughout the 1990s. Since significant use of the Internet by the general public did not occur until the middle of the decade, Roseville compared average local call holding time on its network from 1990-93 with the average holding times of 1998 and 1999. The average holding time for 1990-93 was 3.90 minutes. The average holding time for the years 1998 and 1999 was 6.35 minutes. Roseville also reviewed the traffic studies described above to research the average holding time of local calls transported to identified ISPs. The average holding time for this traffic was approximately 25 minutes. The 63 percent increase between overall average 3.90 minute holding time for 1990-93 and the overall average holding time of 6.35 minutes for 1998-99 appears to be attributable to the substantial use of the network for dial-up calls to the Internet.

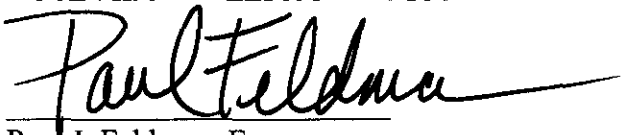
at that time would a rate be designed to recover the new revenue requirement. Any other approach ignores long standing industry practices and would turns logic on its head.

V. Conclusion

Of all of the companies impacted by separations policy, only one opposed Roseville's PFR. Yet, as demonstrated herein, Verizon's argument regarding the availability of reliable data is unpersuasive, its assertion regarding the impact of broadband is speculative and misplaced, and the assertion that the costs of delivering traffic to the Internet are recovered through local rates is just not correct. Accordingly, the Commission should grant the Roseville PFR, reduce the local DEM level to reflect actual usage of the local network for ISP-bound traffic, and shift that amount to the interstate DEM. At very least, the Commission should make the default adjustments recommended by the Joint Board.

Respectfully submitted,

ROSEVILLE TELEPHONE COMPANY



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Its Attorney

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April 10, 2002

ATTACHMENT 1

Excerpts from Brief of Verizon California Inc.

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA
-oOo-

Order Instituting Rulemaking on the Commission's Own Motion into Reciprocal Compensation for Telephone Traffic Transmitted to Internet Service Providers' Modems.	)	R.00-02-005

OPENING BRIEF OF VERIZON CALIFORNIA INC. (U 1002 C)

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Dated: September 18, 2000

Table of Contents

I.

INTRODUCTION AND EXECUTIVE SUMMARY

In the Order Instituting Rulemaking (OIR) that commenced this proceeding, the California Public Utilities Commission (Commission) sought information to determine whether it should revise its rules concerning the application of reciprocal compensation to traffic delivered to internet service providers (ISPs).[1] Verizon California Inc. (U 1002 C) (Verizon) appreciates the Commission's willingness to look closely at this critically important issue.

The Commission's present rules afford identical treatment to traffic delivered to ISPs and to standard local plain old telephone service (POTS) customers. Specifically, the Commission has applied the reciprocal compensation provisions of applicable interconnection agreements equally to both types of traffic.[2] The record developed in this proceeding demonstrates that the Commission's existing policy on reciprocal compensation ignores fundamental differences between the two types of traffic, distorts competition in a variety of harmful ways, and imposes large unrecoverable costs on incumbent local exchange carriers (ILECs) and corresponding windfalls on interconnected competitive local exchange carriers (CLECs).

As discussed in detail in Section II.A., calls to ISPs differ in several fundamental respects from local calls to POTS customers. There are differences in the equipment that is used to "terminate" the two types of calls, differences in how the calls are processed by the equipment used, and differences in the traffic characteristics of the two types of calls.

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[1] See Order Instituting Rulemaking at 6-9.

As discussed in Section II.B., these differences are not merely of academic interest. They are real-world differences that have a dramatic impact on the usage-sensitive costs an interconnected carrier incurs to deliver the traffic its customer. The upshot of these differences is that the traffic-sensitive cost of delivering dial-up traffic to an ISP is a small fraction of the cost of delivering local voice traffic to a standard POTS customer.

Thus, for the last several years, the Commission's rule treating the two types of traffic as the same has provided CLECs – who can target ISPs and avoid serving customers that originate dial-up ISP-bound traffic – a large and unearned windfall. This windfall has, of course, been paid for by the ILECs – principally Verizon and Pacific Bell (Pacific) – that have no choice but to serve the originating customers and to interconnect with CLECs that have inserted themselves between the ILECs and the ISPs. Indeed, over a recent 18-month period, this regulatory regime has cost Verizon approximately $27 million – an amount that will continue to grow, most likely at an accelerating rate.[3] The costs incurred by Pacific are even larger, totaling $173 million through early 2000.[4]

Although the cost the ILECs incur to subsidize the CLECs is the direct result of the Commission's regulatory mandate, the Commission has not provided any mechanism for the ILECs to recover the cost of this subsidy. Because most of Verizon's customers that originate dial-up traffic to ISPs – predominantly residential customers – take service under flat rates, it is impossible for Verizon to recover the

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2 See D.98-10-057, as modified by, D.99-07-047.

3 Ex. 78 (Verizon/Beauvais) at 30.

4 Ex. 15 (Pacific/Jacobsen) at 15.

usage-sensitive reciprocal compensation charges that arise as a result of the Commission's policy.[5] Given the volume of minutes that such customers send to the Internet, this mismatch between the intercompany compensation structure and end user rates is no trifling matter. As discussed in Section II.C. below, the intercompany compensation payment that Verizon must make for a residential customer that uses her line to make dial-up calls to her ISP can easily consume half of the total monthly payment that the customer pays for local telephone service.

The record also demonstrates that the Commission's existing policy of imposing above-cost reciprocal compensation payments for ISP-bound traffic without providing any recovery mechanism produces a variety of undesirable policy effects. As discussed in detail in Section II.C. – and as the Colorado Commission recently found in an analogous proceeding[6] – this regulatory regime:

- Discourages CLECs from serving all customers – including residential customers – who originate dial-up traffic to ISPs;
- Reduces incrementally the incentive for CLECs to deploy advanced services – which are not subject to reciprocal compensation – to access the Internet;
- Imposes large, unrecoverable costs on ILECs customers; and
- Undermines the efficient growth and integrity of the Internet.

Fundamentally, these undesirable policy impacts are caused by two related aspects of the existing regime: (1) the mismatch between large usage-based reciprocal compensation charges and the existing end-user rate structure faced by the ILECs; and

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[5] See Ex. 78 (Verizon/Beauvais) at 28-31.

[6] Petition of Sprint Communications Company, L.P. for Arbitration Pursuant to U.S. Code § 252(b) of the Telecommunications Act of 1996 to Establish an Interconnection

(2) the existence of POTS-based reciprocal compensation rates that vastly exceed the cost of delivering ISP-bound traffic.[7]

As a theoretical matter, these problems could be solved by sharply reducing the reciprocal compensation rate to reflect the much lower cost of delivering ISP-bound traffic and establishing a mechanism for the ILEC to recover the costs from the cost causer.[8] The Commission could permit carriers to recover their costs by billing the ISP for its customer's usage or by imposing on end users mandatory measured service rates that allow for recovery of reciprocal compensation costs.[9]

Although the first objective – reducing the rate for delivering ISP-bound traffic – may be achievable, neither of the above-mentioned cost recovery mechanisms can be put in place in the near term. The ISP billing approach is arguably prohibited by the Federal Communications Commission's (FCC) existing ISP access-charge exemption, and a shift to mandatory measured service would be a major undertaking that would be certain to face substantial opposition.

Given these realities and the severe inadequacies of the existing regulatory regime, the optimal solution for the near-term is to adopt a preferred policy of bill-and-keep for ISP-bound traffic.[10] This approach would eliminate both the disincentive for CLECs to serve residential customers and to deploy advanced Internet

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Agreement with U.S. West Communications, Inc., Docket No. 00B-011T, Initial Commission Decision at 16-17 (Colo. P.U.C. May 3, 2000).

7 See Ex. 78 (Verizon/Beauvais) at 4-8, 20-32.

8 Ex. 78 (Verizon/Beauvais) at 7-8.

9 Id. at 7-8 and fn. 5.

10 Id. at 4-8.

access technologies.[11] It would also put an end to an existing policy that requires ILECs to subsidize CLECs with above-cost payments, replacing it with a regime that requires each carrier to bear equally the cost of serving its own customers. Absent this change, Verizon will have no choice but to seek an immediate increase in its end-user rates in the second phase of this proceeding. Although Verizon does not want to take this step, it would have no choice given the magnitude of the costs imposed by the existing regulatory mandate and the increasing trajectory of this burden.

To summarize, the record demonstrates that the existing regime has distorted competition and has imposed unwarranted costs on ILECs while providing a corresponding and undeserved windfall to certain CLECs. The Commission must put an end to this regime. Unless and until the FCC reverses the ISP access-charge exemption or this Commission revises ILEC end user rates to accommodate the cost of paying reciprocal compensation for ISP-bound traffic, the fairest and most appropriate solution is to impose bill and keep for ISP-bound traffic.

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[11] Id. at 31-32.

their costs through per-minute fees on end users that dial up to the Internet.[138] Finally, as the USIIA correctly concluded:

> [T]he payment of reciprocal compensation for the termination of calls to Internet Service Providers are inconsistent with the realities of the marketplace, and . . . such payments are detrimental to the growth and integrity of the Internet industry.[139]

D. ISP-Bound Traffic Can Be Segregated From Other Types Of Traffic

In an effort to distract the Commission from the serious policy problems arising from the existing regime, the CLECs argue that, in any event, it is impossible to segregate ISP-bound traffic from other forms of traffic. The record in this proceeding, however, demonstrates it is possible to track ISP-bound traffic with reasonable accuracy.

As Verizon witness Beauvais explains, the average traffic patterns for ISP traffic and local voice traffic are sufficiently distinct to allow a simple algebraic formula to be applied to observed hold-time data to estimate the amount of ISP-bound traffic travelling between any two carriers.[140] Both the published data and Verizon's own observations demonstrate that the average duration of ISP-bound traffic is much longer than the average duration of typical local voice traffic[141] and the standard deviations are such that – even at the 99 percent confidence interval – the confidence intervals do not

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138 See Reply Comments of the US Internet Industry Association, In Re Inter-Carrier Compensation For ISP-Bound Traffic, Federal Communications Commission, CC Docket No. 99-68 at 5-6.

139 Id. at 2. A copy of these comments are attached as Exhibit 2 to this brief. Pursuant to Rule 73 of the Commission's Rules of Practice and Procedure and California Evidence Code Section 452(d), the Commission may take official notice of this pleading as an official record of an adjudicatory agency of the United States.

140 Ex. 78 (Verizon/Beauvais) at 15-16.

141 Ex. 78 (Verizon/Beauvais) at 10.

even come close to overlapping.[142] This rather large difference in average duration means that it is possible, as a statistical matter, to distinguish between these two types of traffic with sufficient precision for the Commission's purposes.

Unable to rebut the contention that it is possible to distinguish between ISP-bound traffic and other types of local traffic as a statistical matter, the CLECs have argued that statistical estimation techniques should not be used to identify ISP-bound traffic because the use of these techniques would result in the misclassification of individual calls. Although it is true that the use of statistical estimation techniques would result in certain individual voice calls being classified as ISP-bound calls and vice versa, that is not in itself a justifiable reason to refrain from using these techniques. The Commission and the CLECs have been willing to use estimation techniques in a variety of circumstances, notwithstanding that the process does not identify each call. For example, existing interconnection agreements between Verizon California and CLECs employ a statistical estimation technique to separate local traffic from toll.[143] The Commission has also used statistical estimation techniques in the context of regulating the electric industry. Using "load profiles" to assign time-of-use charges to customers that only have demand meters.[144] As these examples demonstrate, there is nothing inherently wrong with using estimation techniques to deal with situations where a unit-specific measurement approach is difficult or impractical.

To the extent that the CLECs' concern is really about the accuracy of any specific hold-time estimate, the Commission has at its disposal a simple way to satisfy

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142 Ex. 79 (Verizon/Beauvais) at 17-18.

143 Ex. 79 (Verizon/Beauvais) at 17.

144 Id.

this concern. The Commission could employ conservative hold-time estimates that would tend, if anything, to underestimate the amount of ISP-bound traffic delivered between the parties. This should satisfy any CLEC concerns that a hold-time based traffic estimation approach could result in an underpayment of reciprocal compensation by ensuring that any doubt is resolved in favor of the CLEC.

Assuming, for argument's sake, that estimates based on conservative hold times alone were deemed to be insufficient for some reason, which they should not be, the parties could still segregate ISP-bound traffic from other forms of traffic by conducting traffic studies that sample traffic flowing between the ILEC and the CLEC. Of course, to conduct such studies, it would be necessary to identify by telephone number the ISPs being served by the parties. Although the CLECs suggest that this would be an impossibility, the record in this proceeding demonstrates otherwise. As a threshold matter, the telephone numbers used by ISPs are widely published.[145] Even if they weren't, there is every reason to believe that the parties to this proceeding could readily identify their own ISP customers because carriers need to know whether their customers are ISPs in order to determine how best to serve them.[146] Indeed, the CLECs own Securities and Exchange Commission (SEC) reports – which identify ISP

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145 Tr. 798:15-28 (Focal/Tatak); Ex. 87; Tr. 1001:2-1006:9 (CAISPA/Engdahl); Exs. 100-101.

146 Tr. 194:4-19 (Pacific/Jacobsen) ("Q. So your proposal would be that when a customer comes to a CLEC, that the CLEC essentially require some form of disclosure as to the nature of the calls that are going to be placed over the service that was being purchased? [¶] A. Yes. I don't think that's unreasonable. And in fact, I think it is highly likely that the CLECs would know. [¶] Yesterday we heard that 65 percent of ISPs actually buy an enhanced service from the CLEC in order to have the traffic hauled all the way to the Internet backbone. It is clear that CLECs have a pretty good idea that they are providing service to an Internet service provider. [¶] If they are collocating the modems, if they are offering other enhanced services to them, it only makes sense that these fairly sophisticated users of the telecommunications network would explain to the provider what it is they're doing and what business they're in.")

customers – belie their claims that they cannot identify such customers.[147] In any event, the Commission could require ISPs to identify themselves – just as it requires other customers, such as business and lifeline customers, to identify themselves.[148]

The CLECs have further argued that even if the parties knew which calls were going to an ISP, they would still be unable to determine that every minute of every ISP-bound call terminated out of state. This argument has no merit from a policy perspective because the technology that the carriers use to deliver traffic to ISPs is no more or less costly depending on where the call goes after it reaches the ISP.

It is also irrelevant from a legal perspective whether some portion of any given call involves a connection to an Internet website or server that is located in the same local calling area as the originating caller. When it issued the Declaratory Ruling, the FCC was well aware that not every minute of every ISP-bound call necessarily travels out of state.[149] Nevertheless, the FCC concluded that the Act's reciprocal compensation provision does not apply to ISP-bound traffic, leaving the issue of how to treat such traffic as a matter of policy to the states. As the FCC correctly concluded – and will

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147 Ex. 14 at 5 (We [[Pac-West] are a leading supplier of Internet access and other Internet infrastructure services in California serving 78 Internet service providers, all of which have operations in California, including Concentric Network Corp., EarthLink, Inc. and Splitrock Services, Inc."); Ex. 8 at 1 ("Also, at year-end 1999, the Company [ICG] had . . . approximately 550 ISP customers).

148 Tr. 193:23 – 194:3 (Pacific/Jacobsen) ("[B]ut there is certainly a lot of precedence for us to ask the customer about what kind of customer they are. [¶] We ask customers whether they are business or residence. On private line services we ask the customer whether it is going to be an interstate circuit or an intrastate circuit. We ask customers about Lifeline eligibility. There is a lot of precedence for carriers to find out what the nature of the customer is."]

149 In Re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Inter-Carrier Compensation for ISP-Bound Traffic, Declaratory Ruling in CC Docket No. 96-98, and Notice of Proposed Rulemaking in CC Docket No. 99-68, 14 F.C.C.R. 3689 at ¶ 18 (1999) (hereinafter "Declaratory Ruling"), vacated and remanded, Bell Atlantic v. FCC, 206 F.3d 1 (D.C. Cir. 2000).

likely conclude again on remand – it makes no difference whether a certain subset of the ISP-bound traffic does not travel beyond the local calling area. So long as a "substantial portion" of the traffic travels beyond the local calling scope, it is clear that the federal reciprocal compensation provision is inapplicable.[150]

In any event, the only credible evidence in this case suggests that the vast majority of ISP-bound traffic terminates out of state. Indeed, a typical call to a target Internet website passes through National Access Points for domestic connections, and an additional number of points for international connections. For example, almost all America Online traffic passes through Virginia prior to connection to the Internet.[151] While the CLECs have been able to conjure up hypotheticals under which traffic does not travel over the Internet on an interstate basis – e.g., where the material sought is cached on a local server or the dial-up call is to a bank or an e-mail provider's local server – the CLECs have produced no evidence that these situations are at all common. Indeed, the evidence in the record is to the contrary.[152]

Because there is more than one way to segregate ISP-bound traffic from other forms of traffic with reasonable accuracy, the ability to identify ISP-bound traffic is not the stumbling block that the CLECs suggest. Indeed, this concern would evaporate if the CLECs simply used reasonable diligence to identify their ISP customers.

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150 Id. The Declaratory Ruling is discussed in more detail below in Section II.E.

151 Ex. 138 (Verizon/Jones) at p. 10, ll. 5-18.

152 Tr. 1695:15-25, 1710:25 - 1711:14, 1796:24 - 1797:7 (Pacifc/Harris) (observing that it is typically "uneconomic" for banks to house information on multiple local servers or for ISPs that serve any significant area to house e-mail services on multiple local servers.) Tr. 1623:1-17 (Verizon/Jones) (observing that caching is a "relatively new phenomenon" and that was "at effectively zero" as late as early 1999); Ex. 8 at 7 (ICG 10-K) ("The Company [ICG] estimates that more than 65% ofall of ICG's ISP traffic is routed directly to the Internet.").

III.

CONCLUSION

As the record in this proceeding has made clear, there are fundamental differences between traffic delivered to ISPs and local calls delivered to POTS customers – differences that make the traffic-sensitive cost of "terminating" calls to ISPs vastly lower. For the past several years, certain CLECs have been playing an arbitrage game where they target ISPs and seek to avoid customers that originate dial-up ISP-bound traffic, thus obtaining above-cost payments from the originating ILECs. This game has distorted the competitive marketplace and, in the process, has cost Verizon tens of millions of dollars and Pacific hundreds of millions of dollars. It is time for the Commission to put an end to the reciprocal compensation "boondoggle." Although, as discussed above, a more comprehensive solution to these problems may or may not be attainable in the longer term, the fairest and most practical way to solve

these problems in the near term is to establish bill-and-keep as the preferred treatment for this traffic.

DATED: September 18, 2000

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CERTIFICATE OF SERVICE

I, Joan P. George, a secretary in the law firm of Fletcher, Heald & Hildreth, do hereby certify that a true copy of the *Reply of Roseville Telephone Company to Comments of Verizon on Roseville's Petition for Reconsideration* was sent this 10th day of April, 2002 via United States First Class Mail, postage prepaid, to the following:

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